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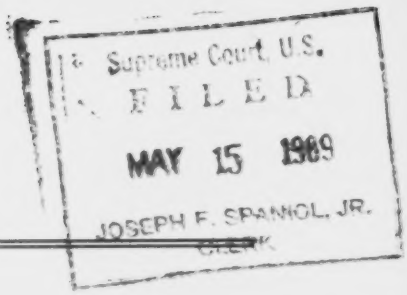

IN THE

Supreme Court of the United States

October Term, 1988

No. -

WILLIAM J. KELLEY,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTION PRESENTED FOR REVIEW

I. Is the holding of the Seventh Circuit that standard instructions on willfulness necessarily encompass an instruction on the defense of reliance on advice of counsel contrary to the opinions of the Supreme Court and contrary to the opinions of the other circuits?

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v.	)
	)
UNITED STATES OF AMERICA, *Respondent.*	)

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

The petitioner, William J. Kelley, respectfully prays that a writ of certiorari issue to review the judgment and decision of the United States Court of Appeals for the Seventh Circuit entered in this proceeding on January 10, 1989.

Opinion Below

The opinion of the Court of Appeals is reported at 864 F.2d 569 (7th Cir. 1989), and it is set forth in the appendix hereto.

Jurisdiction

The jurisdiction of this court is invoked pursuant to 28 U.S.C. 1254(1) for a petition for writ of certiorari to the Court of Appeals. The jurisdiction of the Court of Appeals was invoked pursuant to 28 U.S.C. 1291 as an appeal from a final decision of the district court. The district court had jurisdiction pursuant to 18 U.S.C. 3231 for offenses against the laws of the United States.

The opinion of the Court of Appeals was entered on January 10, 1989. An extension of time within which to file a petition for rehearing was obtained, and a petition for rehearing was timely filed. The Court of Appeals entered an order denying the petition for rehearing on March 15, 1989. This petition for writ of certiorari is timely in that it was filed prior to the expiration of the sixty (60) day period provided by Rule 20 of the Rules of the Supreme Court.

Constitutional and Statutory Provisions Involved

The Fifth Amendment to the United States Constitution and Section 7206(1) and (2) of Title 26 of the United States Code are set forth in the Appendix hereto.

Statement of the Case

William J. Kelley was convicted by a jury of one count of willfully filing a false individual income tax return, in violation of 26 U.S.C. §7206(1). He was also convicted by the jury of eight counts of willfully assisting others in filing false income tax returns, in violation of 26 U.S.C. §7206 (2).

All of the counts arose from one tax shelter investment program known as Stephen Mandarano Fine Arts, Ltd. ("SMFA"). Stephen Mandarano, a person previously unknown to the defendant, owned both SMFA, a New Jersey corporation, and a New Jersey art publishing company called Graphic House. The tax shelter program was promoted to persons across the country by Stephen Mandarano and his associate Alan Bernstein.

The decision of the Court of Appeals described the workings of the tax shelter as follows. Investors bought original lithographic plates from SMFA, along with the rights to the lithograph prints made from the plates and the photo reproductions of the prints (collectively called the "artwork"). Investors paid between $12,500.00 and $18,500.00 in cash and signed a promissory note for the balance of between $155,000.00 and $238,000.00. According to the SMFA offering memorandum, the promissory notes were part recourse and part non-recourse. The investor was personally liable for the recourse portion of the note (approximately one-third of the total note amount), while the non-recourse portion was secured only by the sale of the artwork. The investors assigned distribution rights to the artwork to Graphic House. As Graphic House sold the artwork, 50 percent of the receipts were applied to the recourse portion of the notes. The other 50 percent was retained by Graphic House. According to the offering memorandum, investors could claim depreciation deductions against the cash payments and the recourse portions of the notes each year for seven years following the initial investment.

The problem with the tax shelter, which was later raised by the government, involved the recourse portion of the notes. Prior to 1979, the Internal Revenue Code allowed an investor to base his or her depreciation deductions on financing which was non-recourse. Beginning in 1979, the Code included an "at risk" limitation, which provided that an investor was only entitled to depreciation deductions for the recourse portion of the investor's financing, the portion which the investor was personally liable to repay. *See* 26 U.S.C. §465. The tax shelter, as described above, would have met the at risk requirement and would have allowed investors to claim deductions against the recourse portions of the notes. However, as an inducement to investors who might be reluctant to enter into a contract that exposed them to personal liability, SMFA provided each investor with a "side letter agreement." The letter assured the investor that SMFA would provide a credit for unsold artwork to be applied against the recourse portion of the note. The letter stated that SMFA would never seek any further monies

from investors. The government later claimed and the decision below of the Court of Appeals stated that the credit provided by the letter had the legal effect of destroying the at risk requirement of §465 and thereby had the effect of making the seven year depreciation deductions set forth in the program illegal.

Before notice of any such determination by the government with respect to the tax shelter program, William J. Kelley was advised about the program by an attorney whom he had previously hired for advice on tax shelters, Alfred Brown. Attorney Brown and his law firm were in the business of giving advice to people with regard to income tax shelters as a part of their law practice. The lawyers maintained an office in the same building as the defendant William J. Kelley. Kelley was the owner and operator of Financial Consultants of Indiana, Inc. Kelley had previously hired attorney Brown for advice on tax shelters and had paid him for his services when billed. Later, Kelley asked attorney Brown for advice with regard to another tax shelter. Attorney Brown introduced Kelley to the SMFA program and advised Kelley that the SMFA tax shelter program was a "superior" program to the program about which Kelley had asked. Attorney Brown did not advise Kelley that the credit in the side letter agreement had the legal effect of destroying the at risk requirement of §465 or that the effect was that the seven year depreciation deductions provided by the program were illegal. Attorney Brown recommended the SMFA tax shelter program to defendant Kelley for investment by Kelley and by Kelley's clients. After Alfred Brown advised William J. Kelley about the tax shelter, Kelley invested in the program, and the attorneys in that law firm and Kelley worked together in selling the tax shelters to some of Kelley's financial consulting clients.

In 1979, defendant Kelley purchased an SMFA tax shelter for himself in the conference room of attorney Alfred Brown's law firm. He was also present and assisted in the sale of the same tax shelter program to at least six of his clients. All of the closings took place in the conference room of the law firm.

Present at the closings of Kelley and Kelley's clients were the investor, a representative of SMFA named Alan Bernstein, at least one lawyer of Brown's law firm, and either defendant Kelley or an associate of Kelley. Brown testified that at the closings the investors were told that they should keep the side letter agreement "in a safe place" and avoid showing it to the IRS if they were audited, because otherwise "the tax shelter itself might be in question."

In 1986, the government presented the case to the grand jury and the grand jury returned an indictment against the attorneys Alfred Brown and Steven Goldstein, who were both partners in Brown's law firm. In 1986, both of the lawyers entered pleas of guilty to causing investors to file false income tax returns. Alvin Katzman, another partner in Brown's law firm who also sold the tax shelter program, was not charged by the grand jury. The attorneys had not invested in the tax shelter program themselves. None of the investors were charged by the grand jury.

In 1987, a grand jury returned the indictment in this case against William J. Kelley for filing a false income tax return and causing other investors to file eight false income tax returns. No other investors were charged in the indictment. The government's theory was that because Kelley was a financial consultant, he should have known that the credit provided by the "side letter agreement" presented to him by attorney Alfred Brown and by Mandarano and Bernstein had the legal effect of destroying the recourse portion of the note under §465 and therefore, that the depreciation deductions set forth in the program were illegal. The Court of Appeals held that the evidence was legally sufficient to support jury verdicts of guilty.

The defendant's principal defense before the jury was his reliance on the advice of counsel Alfred Brown. The decision of the Court of Appeals found that whether there was a foundation in the evidence to support the defense theory of good faith reliance was "questionable." The Court of Appeals opinion reviewed the evidence that Brown had served as Kelley's attorney on other matters prior to the SMFA investment, that

Brown reviewed tax shelter investments as part of his law practice, and that Brown introduced Kelley to the SMFA investment. The testimony further showed that Kelley had also sought Brown's advice on a similar investment, that Brown told Kelley that the SMFA investment was superior to the other investment, and that Brown did not tell Kelley that the credit provided by the side letter agreement in the SMFA investment violated the at risk requirement of §465 and that the deductions were therefore illegal.

The opinion also set forth the testimony that Kelley did not pay Brown a retainer for legal advice on the SMFA investment, that Brown and Kelley each travelled separately to New Jersey to view the SMFA artwork and facilities and to discuss the investment with Mandarano and Bernstein. Bernstein testified that he and Mandarano went over all aspects of the program with Kelley, including the offering memorandum and the side letter agreement. Brown testified that at various closings at which Kelley and he were both present, Bernstein would tell the investor that the side letter agreement should be kept secret from the IRS. He testified that he did not tell Kelley about his "concern" about the impact of the side letter agreement on the propriety of the tax deductions because it was apparent at the closings that Kelley was already familiar with the letter. Brown testified that at some of the closings Kelley himself told the client to keep the side letter agreement "in a safe place" and not show it to the IRS.

There was no objection to the admission of the evidence either for or against the defense theory of reliance on the advice of counsel. The defendant tendered an instruction on the good faith reliance on advice of counsel. There was no dispute that the requested instruction was a proper statement of the law. The requested instruction is set forth verbatim in the opinion of the Court of Appeals. App. A-4, 864 F.2d at 572.

The government objected to the giving of an instruction on the defense theory of reliance on advice of counsel on the ground that the defendant had not paid the attorney a retainer. The district court refused to give the requested instruction on reliance on advice of counsel, but permitted the parties to argue the defense to the jury.

The Court of Appeals did not affirm the trial court on the ground that there was no foundation in the evidence for the instruction. Instead, the Court of Appeals stated that whether there was a foundation in the evidence to support the defense theory of good faith reliance on the advice of counsel was "questionable." In footnote 1, the decision of the Court of Appeals recognized that the defendant's attorney argued in the closing argument that the defendant had relied in good faith on attorney Brown's advice regarding the tax consequences of the investment. The footnote stated that "there is no doubt that Kelley's defense theory was presented to the jury." App. A-6, 864 F.2d at 573. However, there was no instruction to the jury on the law as it applied to the defense theory of reliance on the advice of counsel.

The decision of the Court of Appeals assumed that the evidence supported the defense theory of good faith reliance, and went on to hold that general "instructions on willfulness necessarily encompassed Kelley's theory of good faith reliance on counsel's advice." App. A-6, 864 F.2d at 573. The Court of Appeals based its decision on the statement in *United States v. Pomponio*, 429 U.S. 10 (1976), that where a court gives an instruction on the term "willful" in §7206, an additional instruction on general good faith is unnecessary. The Court of Appeals also relied on its own post-*Pomponio* decision of *United States v. Moore*, 627 F.2d 830 (7th Cir. 1980), *cert. denied*, 450 U.S. 916 (1981), which stated the same principal.

REASON FOR GRANTING THE WRIT

I. The holding of the Seventh Circuit that standard instructions on willfulness necessarily encompass an instruction on the defense of reliance on advice of counsel is contrary to the opinions of the Supreme Court and contrary to the opinions of the other circuits.

The decision of the Court of Appeals recognized that good faith reliance on the advice of counsel is a valid defense, and that the defendant in a criminal case is *entitled* to have the jury consider his theory of the defense if there is some foundation in the evidence, however tenuous. The decision stated as follows:

> "Good faith reliance on the advice of counsel is a valid defense to the charge of willfully filing, or willfully assisting others in filing, a false tax return. *United States v. Whyte*, 699 F.2d 375, 379 (7th Cir. 1983). Further, it is well settled that a 'defendant in a criminal case is entitled to have the jury consider any theory of the defense which is supported by law and which has some foundation in the evidence, however tenuous.' *United States v. Grimes*, 413 F.2d 1376, 1378 (7th Cir. 1969); see also *United States v. Boucher*, 796 F.2d 972 (7th Cir. 1986); *United States v. Walsh*, 627 F.2d 88, 93 (7th Cir. 1980); *United States v. Creamer*, 555 F.2d 612, 616 (7th Cir.), *cert. denied*, 434 U.S. 833 (1977)."

App. A-4-5, 864 F.2d at 572.

The Seventh Circuit Court of Appeals held that the general form instructions on willfulness necessarily encompassed an instruction on the defense theory of good faith reliance on counsel's advice. The basis of the holding was the statement in *United States v. Pomponio*, *supra*, that when an instruction on general "willfulness" is given, there is no need to give an instruction on *general* good faith.

Good faith is one element of the defense of reliance on the advice of counsel.The Court of Appeals confused a general good faith defense with the more specific defense of reliance on the advice of counsel.The general good faith defense does not require reliance on anyone.It is not recognized as a defense theory requiring a separate instruction. It is different and separate from the specific defense theory of reliance on the advice of counsel. On the other hand, reliance on the advice of counsel is recognized as a valid defense theory to which an instruction separate from "willfulness" must be given to the jury. Otherwise, the jury is left to consider evidence and arguments of counsel without an instruction on the issue.

The entire reasoning of the Court of Appeals on the issue was stated as follows:

> "Even assuming that the evidence supported the defense theory of good faith reliance, however, we find

> that the instructions, viewed as a whole, adequately encompassed that theory. Willfulness is an element of both 26 U.S.C. §7206(1) and (2). The court's instructions required the jury to find that Kelley acted knowingly and willfully. In defining 'knowingly,' the court required the jury to find that the defendant did not act through ignorance, mistake, or accident. The court defined 'willfully' as 'voluntarily and intentionally with the purpose of avoiding a known legal duty.' In *United States v. Pomponio*, 429 U.S. 10 (1976), the Supreme Court held that the term 'willful' in §7206 means 'a voluntary, intentional violation of a known legal duty,' and that where a trial court so instructs the jury, an 'additional instruction on good faith [is] unnecessary.' *Id.* at 12-13. Similarly, in *United States v. Moore*, 627 F.-2d 830 (7th Cir. 1980), *cert. denied*, 450 U.S. 916 (1981), a case involving failure to file income tax returns in violation of §7203, we stated that a 'jury's conclusion that defendant acted willfully would necessarily negate any possibility of "good faith" in failing to file.' *Id.* at 833. Thus, the court's instructions on willfulness necessarily encompassed Kelley's theory of good faith reliance on counsel's advice.[1]
>
> [1]"In addition, Kelley's attorney argued in closing that Kelley had relied in good faith on Brown's advice regarding the tax consequences of the investment. Thus, there is no doubt that Kelley's defense theory was presented to the jury."

App. A-6, 864 F.2d 573.

The Court of Appeals did not recognize that a general good faith defense is different from the defense of good faith reliance on the advice of counsel. The Court of Appeals simply quoted from *United States v. Pomponio*, *supra*, on general good faith, and stated that therefore, the willfulness instructions encompassed the defense theory of good faith reliance on the advice of counsel.

The instructions on willfulness and knowledge in the *Pomponio* case were fairly complete, making reference to the loans, partnership losses, and deductions. They also instructed that to be found guilty the defendants must be found to have filed a

tax return "willfully and with the specific intent and knowledge at the time they made it that it was in fact a false return." 429 U.S. at 11, fn. 2. There was no instruction given by the trial court in this case requiring such specific intent. The instructions in this case on "knowingly" and "willfully" were general form instructions.

The decision of the Court of Appeals is contrary to the decision of *United States v. Pomponio, supra*, in that *Pomponio* itself recognized that a separate instruction was given on the defense theory in that case. The *Pomponio* decision stated as follows:

> "The trial judge in the instant case adequately instructed the jury on willfulness. An additional instruction on good faith was unnecessary.
>
> "As an alternate ground for ordering a new trial, the Court of Appeals held that respondents were entitled to instructions exonerating them if they believed that the payments to them were loans and that the losses belonged to the partnership, 528 F.2d, at 250. Our inspection of the record indicates that such instructions were given and that they were adequate.[4]
>
> [4]"The instructions set forth in n. 2, supra, by requiring knowledge that the returns falsely reported the transactions, implicitly required knowledge of the true nature of the transactions. In addition, the jury was instructed with respect to the loans that 'if you do find that they were not bona fide loans then you must next determine whether or not the defendants knew at the time they were withdrawing this money that it was not a loan. . . . In other words, you should determine whether they knew that, and as I have told you, that is an essential element. With respect to the partnership losses, the jury was told that the government claimed that respondents 'knew that they couldn't transfer [a certain asset] to a partnership, and, therefore, when they couldn't transfer it they couldn't take the benefits of any losses sustained by the partnership in question. . . ."

429 U.S. at 13. Thus, the *Pomponio* decision does not stand for the principle that a willfulness instruction encompasses a defense theory of the case instruction, but rather, that a willfulness instruction makes a general good faith instruction unnecessary, and that a proper defense theory instruction should be given. The Court of Appeals decision in this case holding that a willfulness instruction encompasses the defense theory instruction of reliance on the advice of counsel is contrary to *Pomponio*.

The *Pomponio* decision was speaking of a general good faith instruction as one negating bad purpose or evil motive. The *Pomponio* decision held that bad purpose and evil motive were not even elements that had to be proven. The court stated that willfulness "simply means a voluntary, intentional violation of a known legal duty." 429 U.S. at 12. Thus, an additional reason that a general good faith instruction is not required to be given is that the court held that bad purpose and evil motive are not required to be proven.

The trial court in this case not only gave just form instructions on knowledge and willfulness, the court gave an instruction that the jury could find knowledge on the part of the defendant if the defendant had a "strong suspicion" but closed his eyes for fear of what he would learn. Instruction Number 11 stated as follows:

> "You may infer knowledge from a combination of suspicion and indifference to the truth. If you find that a person had a strong suspicion that things were not what they seemed or that someone had withheld some important facts, yet shut his eyes for fear of what he would learn, you may conclude that he acted knowingly, as I have used that word."

Such an instruction is the other side of the requested instruction on reliance on the advice of counsel. The government's half of the law was given to the jury, but the defendant's half was not given. Additionally, the giving of the "strong suspicion" instruction was error because it did not include language that the avoidance or shutting of eyes must be "deliberate" or

"willful" and with an absence of actual belief in the legality. *United State v. Lanza*, 790 F.2d 1015 (2d Cir.), *cert. denied*, ___ *U.S.* ___, 107 S. Ct. 211 (1986); *United States v. Arbizo*, 833 F.2d 244 (10th Cir. 1987); *United States v. Cano*, 702 F.2d 370, 371 (2d Cir. 1985); *United States v. Jewell*, 532 F.2d 697 (9th Cir.), *cert. denied*, 426 U.S. 951 (1976).

If the jury is not instructed as to the law applicable to the defense theory of reliance on the advice of counsel, the jury is left to decide a case without being told what the law provides. They may reasonably conclude that if it is not in the instructions given to them by the judge, it has no legal basis. On the other hand, to assume that the jury can be told by the government lawyer or the defense lawyer what the law provides and does not provide, is contrary to our legal procedures and invites confusion before the jury as to the provisions of the law. Thus, it is not good in any respect for the court to fail to instruct the jury on the law as it relates to the defense theory.

The decisions of the Supreme Court have consistently stated that a defendant is entitled to have the trial court instruct the jury on the theory of his defense and that general "conscious participation" instructions are not sufficient. In *United Brotherhood of Carpenters and Joiners of America v. United States*, 330 U.S. 395 (1947) , the court held that general "conscious participation" instructions do not encompass instructions on the liability of a defendant for the actions of others. The instruction on reliance on the advice of someone else such as an attorney is like an instruction on the liability of a defendant for the actions of someone else. General "conscious participation" instructions do not encompass the law on liability for the actions of others or the law on the reliance on the advice of others.

In *Bird v. United States*, 180 U.S. 356 (1901), the Court held that an instruction that murder must be "malicious, premeditated, and willful, and that said killing was not in the necessary defense of the defendant's life" was insufficient and reversible because it did not instruct as to the defendant's belief that his life was in danger. 180 U.S. at 361. Again, general instructions on "willful" were not sufficient to inform the jury as to the law

on the defense theory which was being litigated before the jury. The Court stated the importance of an instruction on the theory of the defense as follows:

> "It is well settled that the defendant has a right to a full statement of the law from the court, and that a neglect to give such full statement, when the jury consequently fall into error, is sufficient reason for reversal. The numerous decisions to this effect are cited in Wharton on Criminal Law, Vol. 3, §3162, 7th ed. The chief object contemplated in the charge of the judge is to explain the law of the case, to point out the essentials to be proved on the one side and the other, and to bring into view the relations of the particular evidence adduced to the particular issues involved."

180 U.S. at 361.

Williamson v. United States, 207 U.S. 425 (1907), involving a charge against a congressman and others for subordination of perjury, noted that the trial court gave a good faith instruction as well as an instruction on reliance on advice of counsel. The Court found without discussion that the instructions were a sufficient statement of the law. As the complexity of the income tax laws increased, decisions began to be reported in criminal income tax cases involving the defense of reliance on advice of counsel. *United States v. McCormick*, 67 F.2d 867 (2nd Cir. 1933), *cert. denied*, 291 U.S. 662 (1934). More recent decisions have refined the instruction language, requiring that the advice of counsel must be after a full disclosure of the facts and that the reliance on the advice by the defendant must be in good faith. See, e.g., *United States v. Whyte*, 699 F.2d 375 (7th Cir. 1983).

The decision below of the Court of Appeals for the Seventh Circuit changes the law of the circuit. *United States v. Phillips*, 217 F.2d 435 (7th Cir. 1954) held that the defendant was entitled to an instruction on the good faith reliance on advice of counsel. General instructions on willfulness were given, but they were insufficient to instruct on the reliance defense. The same arguments were made in that case which were made in this case, and the decision stated as follows:

> "An argument to a jury, however, on a legal issue, unsupported by an instruction to which the defendant was entitled, constitutes an aggravation rather than a mitigation of the harmful effect of the court's refusal to instruct. The government relies upon the well established rule that the instructions must be considered as a whole and, when so viewed, the jury was amply instructed on the issue of good faith. This argument does nothing more than beg the question under discussion. Particularly is this so when the court instructed the jury, 'Nor would mere negligence or carelessness, unaccompanied by bad faith, render the defendant guilty under the six counts.' The jury was thus instructed, notwithstanding there was no contention and no proof that the defendant failed to report total gross income through either negligence or carelessness, but the court refused to instruct as to the effect which the jury might ascribe to the government's proof that his failure to so report was occasioned by the advice which he had received from his lawyer."

217 F.2d at 440-441. A reliance on advice of counsel instruction which required full disclosure of all facts was found sufficient in the decision of *United States v. Baldwin*, 307 F.2d 577 (7th Cir. 1962), *cert. denied*, 371 U.S. 947 (1963). *United States v. Whyte*, 699 F.2d 375 (7th Cir. 1983), followed *Baldwin* and found sufficient a "reliance defense instruction" on advice of an accountant which required full disclosure.

United States v. Davenport, 824 F.2d 1511 (7th Cir. 1987) found that the jury was correctly instructed as to the term "willful" as required by *United States v. Pomponio*, *supra*, and that the jury was correctly instructed in conformance with *Baldwin* in a separate instruction on reliance on advise of counsel. 824 F.2d at 1511. The *Davenport* decision stated as follows:

> "The jury was fully and correctly instructed on the 'willful' requirement as a voluntary, intentional violation of a known legal duty. *United States v. Pomponio*, 429 U.S. 10, 12, 97 S.Ct. 22 p 23, 50 L.Ed.2d 12 (1976). The defendant did not object to that instruction.

> "The jury was then instructed on the defendant's theory of his defense to the effect that he claimed to have relied in good faith on attorney Hyde's advice and therefore what he did was not willful. We find no fault with that instruction as it relates to reliance on the advice of an attorney. *United States v. Baldwin*, 307 F.2d 577, 579 (7th Cir. 1962), *cert. denied*, 371 U.S. 947, 83 S.Ct. 501, 9 L.Ed2d 497 (1963); *United States v. Samara*, 643 F.2d 701, 703 (10th Cir.), *cert. denied*, 454 U.S. 829, 102 S.Ct. 122, 70 L.Ed.2d 104 (1981)."

824 F.2d at 1517.

The decision of the Court of Appeals for the Seventh Circuit in this case not only changes the law of the circuit, but also creates a split in the decisions of the circuit courts of appeal. The Sixth Circuit decision of *United States v. Duncan*, 850 F.2d 1104 (6th Cir. 1988), considered exactly this issue with reference to good faith reliance on a tax accountant. The Sixth Circuit held that a general willfulness instruction does not encompass a proper instruction on reliance on the advice of a tax accountant. The Sixth Circuit relied on the Seventh Circuit decision of *United States v. Phillips*, 217 F.2d 435 (7th Cir. 1954), and stated as follows:

> "Reversing the conviction, the Seventh Circuit noted that counsel's reliance argument to the jury, unsupported by an appropriate instruction, constituted 'an aggravation rather than a mitigation of the harmful effect of the court's refusal to instruct.' *Id.* at 440.
>
> "The same is true here. The District Court's general willfulness instruction enumerated for the jury three specific instances in which conduct would not be willful: 'if it results from [1] negligence, however great, [2] inadvertence or mistake or [3] due to a good faith misunderstanding of the law.' Tr. 1954. Only the interest deduction could fit into these categories as due to 'inadvertence or mistake.' There was no claim that Duncan's actions on the interest item were due to either negligence or misunderstanding of the law, and no claim that his actions on the capital gain fell into any of the three categories listed. Even if the jury accepted as factually established the

> reliance arguments made by Duncan's counsel, it could not match those arguments against any of the trial judge's categories of exception. The boilerplate instruction on willfulness given by the District Court thus could not have been cured by argument of counsel. To the contrary, the jury might well have concluded that counsel's hollow argument on reliance was contrary to, and precluded by, the judge's statement of the law."

850 F.2d at 1118. The Sixth Circuit suggested that the trial court could combine a reliance instruction with a "willful blindness" instruction when the evidence supports such instructions. The district court in petitioner's case gave a "strong suspicion" instruction, did not give a "willful blindness" instruction, and refused to give an instruction on reliance on advice of counsel.

The Second Circuit in a case charging failure to file tax returns held that the defendant was entitled to an instruction submitting his theory that his accountant led him to believe that an extension had been granted. *United States v. Platt*, 435 F.2d 789 (2nd Cir. 1970). The conviction was reversed and remanded for new trial even though an instruction on "willful" was given.

The Fourth Circuit in *United States v. Mitchell*, 495 F.2d 285 (4th Cir. 1977), and *United States v. Miller*, 658 F.2d 235 (4th Cir. 1981), held that general willfulness instructions do not encompass a reliance defense. The more recent *Miller* decision stated as follows:

> "Although the district court conscientiously strove to instruct the jury fairly and fully, we are not persuaded that the charge when read in its entirety explained Miller's defense adequately. Instructing a jury that the government must prove that a defendant intended to commit an offense is quite different from explaining to the jury how the defendant can legitimately counter the government's proof of this essential element of the crime. Our precedent on this point establishes that a district court's charge to the jury must be 'sufficiently precise to instruct the jury in the defendant's theory of defense.' *United States v. Mitchell*, 495 F.2d 285, 288 (4th Cir. 1977). There

> we reversed a judgment of conviction for tax evasion because the district court did not give a precise and specific charge on the reliance defense. Oblique references to the defense, we held, were insufficient. Other authorities hold that despite a general instruction on intent, it is reversible error not to give a specific instruction on the reliance defense when a proper foundation has been laid. *See Bursten v. United States*, 395 F.2d 976, 981-82 (5th Cir. 1968)."

658 F.2d at 237.

In *Bursten v. United States*, 395 F.2d 976 (5th Cir. 1968), the Fifth Circuit held that general instructions on willfulness are not sufficient when the issue presented to the jury is reliance on the advice of counsel. The decision noted that when the trial judge fails to instruct on a defense, he removes the issue from the jury and directs a verdict on that issue against the defendant. The decision stated as follows:

> "While the record reveals (Tr. 795-798) that the trial judge gave a general instruction to the jury on the element of intent, the authorities cited and quoted from conclusively hold that appellant was entitled to a more specific charge in light of his contention that he relied on advice of his tax counsel. This failure to give such a specific charge, even though it should have been reworded, so as to indicate that, to rely on this defense, appellant should have been found to have given all the facts to his advisor, was reversible error."

395 F.2d at 982. *United States v. Musgrave*, 444 F.2d 755 (5th Cir. 1971), held that the chairman of a savings and loan association charged with making loans on false valuation reports was entitled to an instruction on reliance on advice of counsel as well as general instructions.

The decisions of the Fifth Circuit and other circuits have stated that the defense theory of good faith reliance on the advice of counsel requires that the counsel be competent. Reliance cannot be placed on a tax protestor seminar. *United States v. Anderson*, 577 F.2d 258 (5th Cir. 1978). Reliance cannot be placed on a tax protestor attorney whom the defen-

dant has sought out because he agreed with defendant's antitax sentiments, not because the defendant was seeking competent legal advice. *United States v. Farber*, 630 F.2d 569 (8th Cir. 1980), *cert. denied*, 449 U.S. 1127 (1981). Reliance cannot be placed on a disbarred attorney. *United States v. Barney*, 674 F.2d 729 (8th Cir.) , *cert. denied*, 457 U.S. 1139 (1982); *United States v. Hoopes*, 545 F.2d 721 (10th Cir. 1976), *cert. denied*, 431 U.S. 954 (1977). The last three decisions involved one attorney named William Drexler. Disobeyance of a court order on the reliance on the advice of a tax accountant is not a good faith reliance. *Steinert v. United States*, 571 F.2d 1105 (9th Cir. 1978).

There must be a foundation in the evidence for the instruction, and several decisions have denied the giving of a reliance instruction on the ground that the evidentiary foundation was insufficient. *See, e.g., United States v. Snyder*, 766 F.2d 167 (4th Cir. 1985) (several attorneys whose full names the defendant could not remember); *United States v. Samara*, 643 F.2d 701 (10th Cir.) , *cert. denied*, 454 U.S. 829 (1981) (defendant concealed facts).

One decision of the Fifth Circuit stated that a requested instruction stating that reliance is a complete defense was a statement contrary to law, but the decision does not describe how it was contrary. *United States v. Venditti*, 533 F.2d 217 (5th Cir. 1976). Another Fifth Circuit decision noted that the reliance instruction was set forth verbatim within an instruction on "willfully." *United States v. Austin*, 774 F.2d 99, 102-103, fn. 1 (5th Cir. 1985).

The Ninth Circuit in *United States v. Pallan*, 571 F.2d 497 (1978), *cert. denied*, 436 U.S. 911 (1978), held that an instruction on tax evasion and false return charges which instructed that they "require proof of specific intent before the defendant can be convicted" properly instructed the jury on the defendant's theory of reliance on his tax advisor. Not many facts are given in that decision about the tax advisor or the reliance, so the full meaning of the decision cannot be ascertained. In William J. Kelley's case, the court did not even instruct that specific intent was required.

The decision below sets the precedent in the Seventh Circuit and in any other circuit which wishes to adopt it for the denial to the jury of any instruction of law on the defense of reliance on the advice of counsel in any case in which form instructions are given on general "willfulness." Since willfulness is an element of most of the serious federal crimes, and since an instruction on general "willfulness" is given in most serious federal criminal cases, the effect of the decision has wide ranging impact. It affects most serious federal criminal cases. No instruction of law would be given to the jury on the defense theory of reliance on advice of counsel in any of those cases. Furthermore, no instruction of law would be given to the jury on similar defense theories on the same reasoning that form instructions on general "willfulness" encompass those defense theories. The juries would be without an instruction of law on the most important issues litigated before them. The reasoning of the Court of Appeals for the Seventh Circuit does not make any sense. It creates enormous problems.

The only reason for the decision, the only reason for the change in position of the Seventh Circuit, and the only reason for the creation of the split in the circuits is the misreading of this court's *Pomponio* decision. Only the Supreme Court can remedy this misreading and prevent the enormous problems.

The decision of the Court of Appeals is contrary to the decisions of the Supreme Court on the entitlement of a separate instruction on a valid defense theory and the decision creates a split in the circuits as to the entitlement to a separate instruction on reliance on advice of counsel. There is no reason for not giving juries a proper instruction of the law. There is every reason to grant the petition for writ of certiorari to the Court of Appeals for the Seventh Circuit.

The Court may also decide in its discretion that summary reversal and remand to the Court of Appeals is appropriate.

It is difficult for the petitioner to understand how there could be no evidentiary basis for the giving of the requested instruction when the trial court and the Court of Appeals found that the issue was "presented to the jury." App. A-6, 864 F.2d at

573. However, the court may reverse and remand to the Court of Appeals to determine the issue which it did not decide, that is, whether there was an evidentiary basis for the giving of the requested instruction.

Conclusion

For all of the foregoing reasons, the petition for a writ of certiorari should be granted. The court should hold that a form instruction on willfulness does not encompass a defense theory of reliance on the advice of an attorney. The decision of the Court of Appeals should be reversed and the case remanded to the Court of Appeals.

Respectfully submitted,

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In the

United States Court of Appeals

For the Seventh Circuit

No. 88-1231

UNITED STATES OF AMERICA,

Plaintiff-Appellee,

v.

WILLIAM J. KELLEY,

Defendant-Appellant.

Appeal from the United States District Court
for the Southern District of Indiana, Indianapolis Division.
No. IP 87-48-CR—**James E. Noland**, *Judge.*

ARGUED SEPTEMBER 13, 1988—DECIDED JANUARY 10, 1989

Before POSNER, FLAUM, and MANION, *Circuit Judges.*

FLAUM, *Circuit Judge.* Defendant-Appellant William Kelley was convicted by a jury in the Southern District of Indiana on one count of willfully filing a false individual income tax return, in violation of 26 U.S.C. § 7206(1), and eight counts of willfully assisting others in filing false income tax returns, in violation of 26 U.S.C. § 7206(2). Kelley appeals from the judgment of conviction asserting that: (1) the district court erred in refusing to give a tendered instruction on good faith reliance on advice of counsel; (2) the district court erred in admitting into evidence certain statements pursuant to Federal Rule of Evidence 801(d)(2)(e); (3) the district court erred in failing to dismiss the eight counts under § 7206(2) as barred by

the statute of limitations; (4) there was insufficient evidence to support the convictions; (5) the district court erred in admitting an exhibit into evidence; and (6) the district court erred in refusing to give a tendered instruction on first amendment protection of advocacy. For the reasons stated in this opinion, we affirm the judgment of conviction.

I.

This case concerns a tax shelter investment known as Stephen Mandarano Fine Arts, Ltd. ("SMFA"). Stephen Mandarano owned both SMFA, a New Jersey corporation, and a New Jersey art publishing company called Graphic House. The tax shelter worked as follows. Investors bought original lithographic plates from SMFA, along with the rights to the lithograph prints made from the plates and the photo reproductions of the prints (collectively, "artwork"). Investors paid between $12,500 and $18,500 in cash and signed a promissory note for the balance of between $155,000 and $238,000. According to the SMFA offering memorandum, the promissory notes were part recourse and part non-recourse—*i.e.*, the investor was personally liable for the recourse portion of the note (approximately one-third of the total note amount), while the non-recourse portion was secured only by the sale of the artwork. The investors assigned distribution rights to the artwork to Graphic House. As Graphic House sold the artwork, 50% of the receipts were applied to the recourse portion of the notes; the other 50% was retained by Graphic House. According to the offering memorandum, investors could claim depreciation deductions against the cash payment and the recourse portions of the notes each year for seven years following the initial investment.

The problem with the tax shelter involved the recourse portion of the notes. Prior to 1979, the Internal Revenue Code allowed an investor to base her depreciation deductions on financing which was non-recourse. Beginning in 1979, the Code included an "at risk" limitation, which provided that an investor was only entitled to depreciation

deductions for the recourse portion of her financing—*i.e.*, for the portion which she was personally liable to repay. *See* 26 U.S.C. § 465. The tax shelter, as described above, would have met the at risk requirement and would have allowed investors to claim deductions against the recourse portions of the notes. However, as an inducement to investors who might be reluctant to enter into a contract that exposed them to personal liability, SMFA provided each investor with a "side letter agreement" that, in effect, negated personal liability on the recourse portion of the notes. The letter assured the investor that SMFA would provide a credit for unsold artwork to be applied against the recourse portion of the note. The letter stated that SMFA would never seek any further monies from investors. The letter destroyed the at risk requirement of § 465 and thereby made the planned deductions illegal.

Defendant William Kelley, owner of Financial Consultants of Indiana, Inc., was one of several promoters of the SMFA tax shelter in Indiana. Other promoters included: Raymond Dudek, an associate in Kelley's firm; and Alfred Brown, Steven Goldstein, and Alvin Katzman, partners in an Indiana law firm ("Brown's law firm"). All of these promoters maintained their offices in the same building and worked together in selling the tax shelters.

In 1979, Kelley purchased an SMFA tax shelter for himself and sold the shelter to at least six of his clients. All of the closings took place in the conference room of Brown's law firm. Present at the closings were the investor, a representative of SMFA named Alan Bernstein, at least one representative of Brown's law firm, and either Kelley or Dudek. Brown testified that at the closings the investors were told that they should keep the side letter agreement "in a safe place" and avoid showing it to the IRS if they were audited, because otherwise "the tax shelter itself might be in question."

As a result of this tax shelter scheme, Alfred Brown, Steven Goldstein, and Alan Bernstein each pled guilty to one count of 26 U.S.C. § 7206(2), aiding and assisting in

the filing of a false tax return. Kelley went to trial on nine counts: one count of 26 U.S.C. § 7206(1), based on his 1981 individual tax return, and eight counts of 26 U.S.C. § 7206(2), based on the 1980 and/or 1981 tax returns of the six clients to whom he had sold the tax shelters. He was convicted on all counts.

II.

On appeal, Kelley first argues that the district court erred in refusing to give his tendered instruction on good faith reliance on advice of counsel. Kelley had testified at trial that attorney Alfred Brown introduced the SMFA tax shelter to him, recommended that it was a "superior" investment, and never told Kelley that the side letter agreement violated the at risk requirement of § 465. Kelley's proposed instruction read as follows:

> If you find that attorney Alfred Brown was fully informed of all relevant facts and advised William J. Kelley that the Stephen Mandarano Fine Arts tax deductions were lawful and proper, and if you find that William J. Kelley relied on that advice, then you may use that as a factor in assessing William J. Kelley's good faith or lack of intent to violate the tax laws.

Kelley claims that the court's refusal to give the instruction denied him the right to have his defense theory presented to the jury.

Good faith reliance on the advice of counsel is a valid defense to the charge of willfully filing, or willfully assisting others in filing, a false tax return. *United States v. Whyte*, 699 F.2d 375, 379 (7th Cir. 1983). Further, it is well settled that a "defendant in a criminal case is entitled to have the jury consider any theory of the defense which is supported by law and which has some foundation in the evidence, however tenuous." *United States v. Grimes*, 413 F.2d 1376, 1378 (7th Cir. 1969); *see also United States v. Boucher*, 796 F.2d 972 (7th Cir. 1986); *United States v. Walsh*, 627 F.2d 88, 93 (7th Cir. 1980); *United States*

v. Creamer, 555 F.2d 612, 616 (7th Cir.), *cert. denied*, 434 U.S. 833 (1977). This is not to say, however, that the defendant is entitled to a particular instruction. Rather, the defendant is entitled only to have his *theory*, if supported by the evidence, considered by the jury. *See United States v. Douglas*, 818 F.2d 1317, 1320 (7th Cir. 1987); *Boucher*, 796 F.2d at 976. The questions on appeal, then, are whether the evidence supported Kelley's theory of good faith reliance on advice of counsel and, if so, whether the court's instructions, viewed as a whole, encompassed that theory.

Whether there was a foundation in the evidence to support the defense theory of good faith reliance is questionable. The testimony of Brown and Kelley at trial showed only that Brown had served as Kelley's attorney on other matters prior to the SMFA investment, that Brown reviewed tax shelter investments as part of his law practice, that Brown introduced Kelley to the SMFA investment, that Brown told Kelley that the SMFA investment was superior, in the sense of more profitable, than another investment they had discussed, and that Brown did not tell Kelley that the side letter agreement violated the at risk requirement of § 465. To place this testimony in perspective, we also note the following. Kelley testified that he did not retain Brown for legal advice on the SMFA investment. Brown and Kelley each travelled separately to New Jersey to view the SMFA artwork and facilities and to discuss with Mandarano and Bernstein the investment. Bernstein testified that he and Mandarano went over all aspects of the program with Kelley, including the offering memorandum and the side letter agreement. Brown testified that at various closings at which Kelley and he were both present, Bernstein would tell the investor that the side letter agreement should be kept secret from the IRS. He testified that he did not tell Kelley about his "concern" about the impact of the side letter agreement on the propriety of the tax deductions because it was apparent at the closings that Kelley was already familiar with it. Brown testified that at some of the closings Kelley

himself told the client to keep the side letter agreement "in a safe place" and not show it to the IRS.

Even assuming that the evidence supported the defense theory of good faith reliance, however, we find that the instructions, viewed as a whole, adequately encompassed that theory. Willfulness is an element of both 26 U.S.C. § 7206(1) and (2). The court's instructions required the jury to find that Kelley acted knowingly and willfully. In defining "knowingly," the court required the jury to find that the defendant did not act through ignorance, mistake, or accident. The court defined "willfully" as "voluntarily and intentionally with the purpose of avoiding a known legal duty." In *United States v. Pomponio*, 429 U.S. 10 (1976), the Supreme Court held that the term "willful" in § 7206 means "a voluntary, intentional violation of a known legal duty," and that where a trial court so instructs the jury, an "additional instruction on good faith [is] unnecessary." *Id.* at 12-13. Similarly, in *United States v. Moore*, 627 F.2d 830 (7th Cir. 1980), *cert. denied*, 450 U.S. 916 (1981), a case involving failure to file income tax returns in violation of § 7203, we stated that a "jury's conclusion that defendant acted willfully would necessarily negate any possibility of 'good faith' in failing to file." *Id.* at 833. Thus, the court's instructions on willfulness necessarily encompassed Kelley's theory of good faith reliance on counsel's advice.[1]

III.

Kelley next argues that the district court erroneously admitted into evidence statements made by Stephen Mandarano to an undercover IRS agent. The agent testified that in December 1982 he posed as a financial consultant and attempted to obtain information on tax shelter invest-

[1] In addition, Kelley's attorney argued in closing that Kelley had relied in good faith on Brown's advice regarding the tax consequences of the investment. Thus, there is no doubt that Kelley's defense theory was presented to the jury.

ments from Mandarano. The agent testified that Mandarano explained the SMFA investment to him, and told the agent that the side letter agreement was to be kept secret and never shown to the IRS. Kelley objected at trial to the admission of this testimony, asserting that Mandarano's statements were hearsay. The district court admitted the testimony, under Fed. R. Evid. 801(d)(2)(e), as statements of a co-conspirator. The district court made the requisite findings under *United States v. Santiago*, 582 F.2d 1128, 1134 (7th Cir. 1978), that it was more probable than not that: 1) the declarant and the defendant were members of a conspiracy; 2) when the hearsay statement was made; and 3) that the statement was in furtherance of the conspiracy. Kelley challenges the district court's findings on all three points.[2]

As to the first requirement, that the declarant and the defendant were members of a conspiracy, we initially note that Rule 801(d)(2)(e) applies not only to conspiracies but also to joint ventures, and that a charge of criminal conspiracy is not required to invoke the evidentiary rule. *United States v. Coe*, 718 F.2d 830, 835 (7th Cir. 1983); *United State v. Regilio*, 669 F.2d 1169, 1174 n.4 (7th Cir. 1981), *cert. denied*, 457 U.S. 1133 (1982). The district court stated that its use of the term "conspiracy" connoted a joint venture. With that noted, we find that there was sufficient evidence to support the district court's finding that Mandarano and Kelley were members of a conspiracy/joint venture. The evidence showed that Mandarano owned SMFA; that Kelley was one of several promoters of the SMFA investment in Indiana; that Kelley travelled to New Jersey and met with Mandarano to discuss the tax shelter before Kelley started promoting it; that Alan Bernstein,

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[2] Kelley alternatively argues that the district court might have erroneously admitted the statements as showing a method of operation. Our reading of the record shows that, although the court at one point mentioned method of operation, the court clearly admitted the statements under Fed. R. Evid. 801(d)(2)(e). *See* Trial Transcript, Vol. IV, pp. 147-48.

an employee of Mandarano, participated in the closings on the sales to Kelley's clients; that Kelley was aware of the side letter agreement; and that, according to Alfred Brown, at some of the meetings and/or closings Kelley told the customer that the letter was to be kept secret from the IRS.

As to the second requirement, that Mandarano's statements were made at the time the joint venture existed, Kelley argues that the evidence showed only that Kelley sold the investments to his clients in 1979, and that there was no evidence that the joint venture continued through December 1982. We disagree. Kelley's clients were filing tax returns each year after 1979, claiming deductions for the SMFA shelters that they had purchased. That was the whole point of the investment. The conspiracy did not end on the day of Kelley's last closing of an SMFA shelter in 1979. Mandarano was still promoting the shelter in 1982, his statements to the undercover agent were to induce him to become an investor and/or promoter of the shelter, Kelley's clients were still claiming deductions, and presumably all members of the conspiracy were still keeping the side letter agreements "in a safe place" in order to avoid jeopardizing the scheme. *See United States v. Diez*, 515 F.2d 892 (5th Cir. 1975), *cert. denied*, 423 U.S. 1052 (1976) (conspiracy to evade paying income tax did not terminate when returns were filed since tax evasion scheme required continued concealment of underlying transactions).

As to the third requirement, that the statements were made in furtherance of the conspiracy, Kelley makes a meritless argument. He asserts that because it was allegedly imperative that his clients keep the side letter agreement secret, Mandarano's telling more persons—namely, the undercover agent—about the side letter agreement could only have hurt, not furthered, the conspiracy.

In sum, the district court properly admitted Stephen Mandarano's statements into evidence.

IV.

Kelley's third argument concerns counts 1 through 8 of the indictment which charged that he assisted others in the filing of false tax returns, in violation of 26 U.S.C. § 7206(2). These counts were based on the 1980 and/or 1981 returns of the six clients to whom Kelley sold the investments. Kelley claims that these counts were barred by the statute of limitations.

The statute of limitations for violations of 26 U.S.C. § 7206(2) is six years, as set out in 26 U.S.C. § 6531(3). The parties are in agreement that an offense under § 7206(2) is committed, and thus the limitation period begins to run, "at the time the return is filed." *United States v. Habig*, 390 U.S. 222, 223 (1968). Kelley argues that the limitation period began to run in 1980 when his clients filed their 1979 tax returns and that the period ended no later than six years from the last of those filings, namely October 15, 1986. He asserts that the charges under § 7206(2), filed on May 27, 1987, were time-barred and that the district court erred in failing to dismiss those charges.

The Government maintains that although the limitation period had elapsed with respect to the offenses committed by the filings of the 1979 tax returns, subsequent offenses were committed when Kelley's clients filed their 1980 and 1981 returns in, respectively, 1981 and 1982. The Government asserts that it is not limited to prosecuting Kelley for only the first filings of his clients' 1979 returns in 1980 but that it can, and timely did, bring charges based on Kelley's clients' subsequent 1980 and 1981 returns that were filed in 1981 and 1982. Kelley responds that under that logic, a defendant could conceivably be prosecuted 13 years after the acts constituting a violation of § 7206(2). For example, had Kelley's clients continued to claim the illegal deductions for seven years, and an offense occurs with the filing of each successive tax return, the six-year statute of limitations added to the seventh year's offense would total 13 years from the time Kelley had advised his clients about the SMFA investment.

It appears that the issue is one of first impression. The parties and the court have found no cases on point. Kelley relies solely on the general proposition that statutes of limitations should be liberally construed in favor of repose. This proposition is based on two rationales: 1) "to bar prosecutions on aged and untrustworthy evidence"; and 2) "to cut off prosecution for crimes a reasonable time after completion." 22 C.J.S. *Criminal Law* § 223. Kelley also points to the fact that the general limitation period for violations of the internal revenue laws is three years and that only certain offenses, including willfully assisting in the filing of false tax returns, are given a six-year limitation period.

Neither the two rationales cited nor the fact that the limitation period for violations of § 7206(2) is six rather than three years persuades us that the charges against Kelley were time-barred. There is no problem here of aged and untrustworthy evidence nor of unreasonable intervals between the time of the offense and the time of prosecution. An offense occurred each time Kelley's clients, acting pursuant to his advice, filed a tax return claiming the illegal deductions. As previously stated, the whole point of the tax shelter was for investors to claim depreciation deductions for seven years. Kelley's clients were in the process of doing just that, until the government stepped in. At no point did Kelley retract his advice and tell his clients that they should stop claiming the illegal deductions.

The government brought charges against Kelley based on the 1980 and 1981 returns of his clients within six years of the filing of those returns. Thus, the charges were timely filed.

V.

Kelley asserts that there was insufficient evidence to support the convictions. He appropriately states this court's standard of review as "whether, after reviewing the evidence in the light most favorable to the prosecution, any

rational trier of fact could have found the essential elements of the crime beyond a reasonable doubt." *Jackson v. Virginia*, 443 U.S. 307, 319 (1979) (emphasis omitted). Kelley claims that there was insufficient evidence on the element of willfulness, reasoning that, although there was sufficient evidence to show that Kelley knew that the side letter agreement took away the investor's obligation to pay back the "recourse" note, the evidence did not go so far as to show that he knew that the side letter agreement made the deductions illegal under the § 465 at risk requirement. We disagree.

Much of the evidence against Kelley has already been recited in the course of this opinion. We reiterate that testimony was introduced at trial that at some of the closings Kelley himself told the investors to keep the side letter agreement secret from the IRS. In addition, we point out that one of Kelley's clients, Dr. Strickland, testified that Kelley explained to him the difference between recourse and non-recourse notes and the change in the tax laws in 1979 that required investors to be at risk. Strickland further testified that Kelley explained to him "that a certain proportion of the investment had to be at risk in order to qualify for tax savings, that the recourse portion of the note represented that portion of the investment that would be at risk, but that, in fact, it was not at risk." The evidence was sufficient for a rational trier of fact to find the element of willfulness beyond a reasonable doubt.

VI.

Over objection at trial, the Government introduced an April 26, 1981 newspaper advertisement which invited attendance at a three-day financial planning seminar conducted by Kelley's corporation, Financial Consultants of Indiana. The advertisement stated that the seminar would be "with William J. Kelley, Raymond J. Dudek, James Brocke" and that topics would include "How the NEW TAX LAWS can help you avoid taxes legally NOW," "How

to get tax-free income," "TAX SAVINGS TECHNIQUES," "How to build A TAX-FREE INCOME," and "Turning your tax liabilities into capital assets." The advertisement noted "30 Years of Financial Planning Experience." Kelley claims that the advertisement was not relevant and that any relevancy was outweighed by its prejudicial effect, citing Fed. R. Evid. 401, 403. Kelley argues that simply because the advertisement stated that the seminar would be "with" William J. Kelley, the advertisement was not relevant to whether Kelley had knowledge of the specific at risk requirement of § 465. We disagree.

At trial, Kelley maintained that he did not act willfully or knowingly. The advertisement was clearly relevant as evidence to rebut his claim of ignorance. Kelley was president of Financial Consultants, actively participated in promoting tax shelters, and advertised his company as having 30 years' experience. The advertisement was placed around the time that Kelley's clients' 1980 tax returns would become due—tax returns that contained illegal deductions taken on the SMFA investment sold to them by Kelley with the advice to keep the side letter agreement "in a safe place." The advertisement shed probative light on the element of willfulness. Moreover, the Government introduced the advertisement only after Kelley specifically testified that his company did not, and never had, provided tax advice. The advertisement is clearly relevant on the issue of Kelley's credibility in denying that his company ever gave tax advice.

As to its prejudicial effect, we review the district court's determination under an abuse of discretion standard. *United States v. Laughlin*, 772 F.2d 1382, 1393 (7th Cir. 1985). The district court did not abuse its discretion in determining that the probative value of the advertisement was not outweighed by its prejudicial effect.

VII.

Kelley's final contention is that the district court erred in rejecting his tendered instruction on first amendment protection of advocacy. The instruction read as follows:

> William J. Kelley is afforded First Amendment protection from prosecution for mere advocacy of a tax shelter program. The First Amendment defense is afforded a defendant who did not actively perform all the organizational and managerial tasks necessary to create and operate the tax shelter.
>
> If you find that William J. Kelley was not closely involved in the creation and operation of the "Stephen Mandarano Fine Arts" tax shelter program, the First Amendment protects him from criminal sanction."

Kelley relies on a line of Ninth Circuit cases to support the giving of this instruction. In *United States v. Dahlstrom*, 713 F.2d 1423 (9th Cir. 1983), *cert. denied*, 466 U.S. 980 (1984), the court held that mere advocacy of a tax shelter program is protected by the first amendment. In that case, the defendants formed a membership organization (the "ALA") that provided advice to members about how to set up foreign trust organizations ("FTO's") as tax shelters. The ALA ran seminars where members were instructed on how to create FTO's. The seminar did not include advice or assistance in tax return preparation, and it was up to each member as to whether he would carry through and create an FTO. Moreover, the legality of an FTO shelter was not settled at the time of the seminars.

In two subsequent cases, the Ninth Circuit has narrowed the *Dahlstrom* holding to find that where a defendant's actions constitute more than mere advocacy, the defendant is not protected by the first amendment. *See United States v. Schulman*, 817 F.2d 1355 (9th Cir.), *cert. denied*, 108 S. Ct. 362 (1987) (defendant created limited partnership and sold partnership interests representing that investment would be deductible; no first amendment protection); *United States v. Solomon*, 825 F.2d 1292 (9th Cir. 1987), *cert. denied*, 108 S. Ct. 782 (1988) (defendants established limited partnerships to purchase patents at inflated prices and sold partnership shares to investors representing that portion of partnership losses would be deductible; no first amendment protection). In each of these cases, the court

noted that the defendants were involved in the creation, organization, and operation of the tax shelters (limited partnerships) at issue. Kelley argues, that because he merely promoted the SMFA shelter but was not involved in creating or operating SMFA, his case is more like *Dahlstrom* than *Schulman* and *Solomon*. He urges us to follow *Dahlstrom* and, further, to find that the evidence supported a first amendment protection of advocacy instruction.

We initially note that we are not bound by Ninth Circuit precedent. Nevertheless, without deciding whether a protection of advocacy instruction would ever be appropriate in a case brought under § 7206, we find that unlike *Dahlstrom*, Kelley did more than merely advocate a tax shelter at a seminar. The evidence showed that he sold the shelter to his clients, advised his clients about the "recourse" portion of the notes, told his clients to keep the side letter agreement secret from the IRS, attended and participated in the closings, and received a commission for each sale. The district court properly rejected the first amendment protection of advocacy instruction.

VIII.

For the reasons stated herein, the judgment of the district court is AFFIRMED.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

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UNITED STATES COURT OF APPEALS

For the Seventh Circuit
Chicago, Illinois 60604

March 15, 1989.

Before
Hon. RICHARD A. POSNER, Circuit Judge
Hon. JOEL M. FLAUM, Circuit Judge
Hon. DANIEL A. MANION, Circuit Judge

UNITED STATES OF AMERICA, *Plaintiff-Appellee,*	)	Appeal from the United States District Court for the Southern District of Indiana, Indianapolis Division.
No. 88-1231 vs.	)	
WILLIAM J. KELLY, *Defendent-Appellant.*	)	No PI 87-48-CR James E. Noland, Judge.

ORDER

On consideration of the petition for rehearing and suggestion for rehearing en banc filed in the above-entitled cause on February 23, 1989, no judge in active service has requested a vote thereon, and all of the judges on the original panel have voted to deny a rehearing. Accordingly,

IT IS ORDERED that the aforesaid petition for rehearing be, and the same is hereby, DENIED.

UNITED STATES COURT OF APPEALS

For the Seventh Circuit
Chicago, Illinois 60604

April 28, 1989.

Before
Hon. JOEL M. FLAUM, Circuit Judge

UNITED STATES OF AMERICA, *Plaintiff-Appellee,*	)	Appeal from the United States District Court for the Southern District of Indiana, Indianapolis Division.
No. 88-1231 vs.	)	
WILLIAM J. KELLY, *Defendent-Appellant.*	)	No 87 CR 48
	)	Judge James E. Noland

This matter comes before the court for its consideration of the following documents:

1. The "MOTION FOR STAY OF MANDATE" filed herein on March 21, 1989, by counsel for the defendant-appellant.
2. The "RESPONSE TO DEFENDANT-APPELLANT'S MOTION FOR STAY OF MANDATE" filed herein on April 17, 1989.
3. The "REPLY TO APPELLEE'S RESPONSE TO MOTION FOR STAY OF MANDATE" filed herein on April 19, 1989.
4. The "MOTION FOR ENLARGEMENT OF THE REQUESTED STAY OF MANDATE" filed herein on April 21, 1989.

On consideration thereof,

IT IS ORDERED that the "MOTION FOR STAY OF MANDATE" is GRANTED and the mandate in this appeal is STAYED to and including May 15, 1989.

DEFENDANT'S TENDERED FINAL JURY INSTRUCTION #2

If you find that attorney Alfred Brown was fully informed of all relevant facts and advised William J. Kelley that the Stephen Mandarano Fine Arts tax deduction were lawful and proper, and if you find that William J. Kelley relied on that advice, then you may use that as a factor in assessing William J. Kelley's good faith or lack of intent to violate the tax laws.

U.S. v. Jernigan (CA FL, 1986), 441 F.2d 471, *cert. denied* 90 S.Ct 262.

WKSC-6.04

INSTRUCTION NO. 10

When the word "knowingly" is used in these instructions, it means that the defendant realized what he was doing and was aware of the nature of his conduct, and did not act through ignorance, mistake or accident. Knowledge may be proved by the defendant's conduct, and by all the facts and circumstances surrounding the case.

WK-9

INSTRUCTION NO. 11

You may infer knowledge from a combination of suspicion and indifference to the truth. If you find that a person had a strong suspicion that things were not what they seemed or that someone had withheld some important facts, yet shut his eyes for fear of what he would learn, you may conclude that he acted knowingly, as I have used that word.

WK-10

INSTRUCTION NO. 12

An act is done "willfully" if done voluntarily and intentionally with the purpose of avoiding a known legal duty.

UNITED STATES CONSTITUTION
AMENDMENT V

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

26 U.S.C. §7206. Fraud and False Statements

Any person who —

(1) Declaration under penalties of perjury. Willfully makes and subscribes any return, statement, or other document, which contains or is verified by a written declaration that it is made under the penalties of perjury, and which he does not believe to be true and correct as to every material matter; or

(2) Aid or assistance. Willfully aids or assists in, or procures, counsels, or advises the preparation or presentation under, or in connection with any matter arising under, the internal revenue laws, of a return, affidavit, claim, or other document, which is fraudulent or is false as to any material matter, whether or not such falsity or fraud is with the knowledge or consent of the person authorized or required to present such return, affidavit, claim, or document; or

. . .

shall be guilty of a felony and, upon conviction thereof, shall be fined not more than $5,000, or imprisoned not more than 3 years, or both, together with the costs of prosecution.

(For offenses committed after September 3, 1982, the penalty reads as follows:)

shall be guilty of a felony and, upon conviction thereof, shall be fined not more than $100,000 ($500,000 in the case of a corporation), or imprisoned not more than 3 years, or both, together with the costs of prosecution.

Supreme Court, U.S.
FILED
JUL 11 1989
JOSEPH F. SPANIOL, JR.
CLERK

No. 88-1864

In the Supreme Court of the United States

OCTOBER TERM, 1989

WILLIAM J. KELLEY, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

KENNETH W. STARR
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QUESTION PRESENTED

Whether the court of appeals erred in upholding the district court's refusal to give a tendered defense instruction on reliance on the advice of counsel under the facts of this tax fraud case.

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In the Supreme Court of the United States

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OPINION BELOW

The opinion of the court of appeals (Pet. App. A1-A14) is reported at 864 F.2d 569.

JURISDICTION

The judgment of the court of appeals was entered on January 10, 1989. A petition for rehearing was denied on March 15, 1989 (Pet. App. A15). The petition for a writ of certiorari was filed on May 15, 1989. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

Following a jury trial in the United States District Court for the Southern District of Indiana, petitioner was convicted on one count of willfully filing a false individual income tax return, in violation of 26 U.S.C. 7206(1), and on

eight counts of willfully assisting others to file false income tax returns, in violation of 26 U.S.C. 7206(2). Pet. App. A1. Petitioner was sentenced to imprisonment for a total of 24 months, with all but four months suspended, and he was fined $5,000. Gov't C.A. Br. 2-3.

Petitioner owned Financial Consultants of Indiana, Inc., a firm that served as financial adviser to numerous professional clients. He was one of several promoters of a tax shelter investment known as Stephen Mandarano Fine Arts, Ltd. (SMFA). Investors in the tax shelter bought original lithographic plates from SMFA, along with the rights to the lithographic prints made from the plates and the photographic reproductions of the prints. The investors paid between $12,500 and $18,500 in cash for the plates and the rights to the prints, and they signed promissory notes for the balance of $155,000 to $238,000. The SMFA offering memorandum represented that the promissory notes were in part recourse and in part non-recourse notes: the investor was personally liable for about one-third of the note amount, while the remainder of the debt was secured only by the sale of prints and reproductions. The offering memorandum also advised that investors could claim depreciation deductions against the cash payment and the recourse portion of the note each year for seven years following the initial investment. Deductions were not allowable for the non-recourse portion, because 26 U.S.C. 465 provides that an investor is entitled to depreciation deductions only for the portion of investment financing that is at risk. Pet. App. A2-A3.

SMFA provided each investor with a "side letter agreement" that effectively negated the investor's personal liability on the recourse portion of the notes. The letter assured the investor that SMFA would provide a credit for unsold artwork to be applied against the recourse portion of the note. The letter also stated that SMFA would never

seek any further monies from investors. The letter therefore made the planned deductions for the "recourse" portion of the notes illegal since the investors were not actually at risk for that portion of the investment. Pet. App. A2-A3.

In 1979, petitioner purchased an SMFA tax shelter for himself and sold the shelter to at least six of his clients. In attendance at each closing were the investor; Alan Bernstein, a representative of SMFA; Alfred Brown, a lawyer and a promoter of the shelter, or another lawyer from his firm; and either petitioner or his associate. Brown testified that at the closings investors were told that they should keep the side letter agreement in a safe place and that they should avoid showing it to the IRS if they were audited, because otherwise "the tax shelter itself might be in question." Pet. App. A3. He further testified that on some occasions petitioner himself "told the client to keep the side letter agreement 'in a safe place' and not show it to the IRS." *Id.* at A6.

Alfred Brown, his associate Steven Goldstein, and Alan Bernstein of SMFA each pleaded guilty to one count of aiding and assisting in the filing of a false tax return in violation of 26 U.S.C. 7206(2). Pet. App. A3. Petitioner went to trial and contended, inter alia, that he had relied in good faith on the advice of counsel. He testified that attorney Alfred Brown had introduced the SMFA tax shelter to him, had recommended it as a "superior" investment, and had never told him that the side letter agreement rendered tax shelter deductions illegal. Pet. App. A4. Petitioner requested an instruction spelling out that defense.[1] The trial court refused to give the instruction.

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[1] Petitioner's proposed instruction read as follows: "If you find that attorney Alfred Brown was fully informed of all relevant facts and advised William J. Kelley that the Stephen Mandarano Fine Arts tax

On appeal, petitioner contended that the court erred in refusing to give his requested "advice of counsel" instruction.[2] The court of appeals disagreed. It first found the existence of an evidentiary foundation for the instruction to be "questionable." Pet. App. A5. It went on to hold that, assuming an evidentiary foundation, petitioner's reliance on counsel theory was adequately encompassed by instructions that the district court had given the jury requiring it to find that petitioner had acted willfully and knowingly. *Id.* at A6.

ARGUMENT

Petitioner contends (Pet. 7-20) that the court of appeals erred in holding that the trial court's instructions on willfulness encompassed his requested instruction on good-faith reliance on the advice of counsel. Review of this issue is not warranted. While the court of appeals charitably characterized the evidentiary foundation for the tendered instruction as "questionable" (Pet. App. A5), the factors to which it pointed establish that there was no evidentiary foundation for the instruction.

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deductions were lawful and proper, and if you find that William J. Kelley relied on that advice, then you may use that as a factor in assessing William J. Kelley's good faith or lack of intent to violate the tax laws." Pet. App. A4.

[2] Petitioner also contended that (1) the district court had erred in admitting certain statements into evidence pursuant to Fed. R. Evid. 801(d)(2)(E); (2) the district court had erred in declining to dismiss the indictment under 26 U.S.C. 7206(2) on the ground that the charges were barred by the statute of limitations; (3) there was insufficient evidence to support the conviction; (4) the district court erred in admitting an exhibit into evidence; and (5) the district court erred in refusing to give a requested instruction on First Amendment protection of advocacy. These contentions are not raised in the petition.

A defendant is not entitled to an instruction on a theory of defense unless he has presented evidence on each element of the defense. See *United States* v. *Bailey*, 444 U.S. 394, 415 (1980). The elements of a valid "advice of counsel" defense are (1) that the defendant honestly and in good faith sought the advice of a competent lawyer, (2) that he made full disclosure of all pertinent facts to the lawyer, and (3) that he followed the advice of the lawyer in good faith, relying on it and believing it to be correct. *Williamson* v. *United States*, 207 U.S. 425, 453 (1908); *United States* v. *Farber*, 630 F.2d 569, 572 (8th Cir. 1980), cert. denied, 449 U.S. 1127 (1981); *United States* v. *Fruehauf Corp.*, 577 F.2d 1038, 1068-1069 (6th Cir.), cert. denied, 439 U.S. 953 (1978); *Bisno* v. *United States*, 299 F.2d 711, 720 (9th Cir. 1961), cert. denied, 370 U.S. 952 (1962).

At trial, petitioner admitted (and Brown likewise testified) that petitioner did not retain Brown for legal advice on the SMFA investment. Moreover, the evidence showed that while Brown did not tell petitioner that the tax shelter deductions were illegal, he likewise did not tell petitioner that they were legal. Brown's statement that the SMFA shelter was "superior" meant only that it was more profitable than another investment he and petitioner had discussed, as the court of appeals noted. Pet. App. A5. Brown testified that it was apparent at the closings that petitioner (who was, after all, the owner of a financial consulting firm) was familiar with the tax problem caused by the side letter agreement. Indeed, Brown testified that petitioner himself told some of the clients not to show the side letter agreement to the IRS. *Id.* at A5-A6. In short, there was no evidence of good faith reliance by petitioner on legal advice sought and obtained from Brown. Rather, the evidence established that petitioner knew that the tax shelter deductions were illegal because of the side letter

agreements and that he and Brown were co-conspirators in a scheme to defraud the government. Thus, there was no evidentiary foundation for the instruction tendered by petitioner, and the trial court properly refused to give it.[3]

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

KENNETH W. STARR
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JULY 1989

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[3] Where there is an evidentiary basis for a defense of reliance on the advice of counsel or a professional tax preparer, courts of appeals have held that an instruction such as the one proposed by petitioner should be given. See *United States* v. *Duncan*, 850 F.2d 1104 (6th Cir. 1988); *United States* v. *Mitchell*, 495 F.2d 285 (4th Cir. 1974); *Bursten* v. *United States*, 395 F.2d 976 (5th Cir. 1968), cert. denied, 409 U.S. 843 (1972). But any error on that score would be harmless under the facts of this case because, as the court of appeals concluded (Pet. App. A6), the instructions, viewed as a whole, did not allow the jury to convict petitioner if it concluded that he had reasonably relied on the advice of counsel. The trial court instructed the jury that, in order to convict, it had to find that petitioner acted knowingly and willfully. It defined "knowingly" to preclude conviction if petitioner had violated the law ignorantly, mistakenly, or accidentally. It defined "willfully" as " 'voluntarily and intentionally with the purpose of avoiding a known legal duty' " (*ibid.*). The jury could not have convicted petitioner under these instructions if it thought that petitioner had somehow relied in good faith on Brown's legal advice. In that event, the jury would have concluded that he had not intentionally violated the law, but had done so mistakenly.

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No. 88-1864 (3)

IN THE

Supreme Court of the United States

October Term, 1989

WILLIAM J. KELLEY, *Petitioner*,

v.

UNITED STATES OF AMERICA, Respondent.

REPLY BRIEF IN SUPPORT OF CERTIORARI

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QUESTION PRESENTED FOR REVIEW

I. Is the holding of the Seventh Circuit that standard instructions on willfulness necessarily encompass an instruction on the defense of reliance on advice of counsel contrary to the opinions of the Supreme Court and contrary to the opinions of the other circuits?

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No. 88-1864

IN THE

Supreme Court of the United States

October Term, 1989

WILLIAM J. KELLEY, *Petitioner*,

v.

UNITED STATES OF AMERICA, *Respondent*.

REPLY BRIEF IN SUPPORT OF CERTIORARI

REASON FOR GRANTING THE WRIT

I. The holding of the Seventh Circuit that standard instructions on willfulness necessarily encompass an instruction on the defense of reliance on advice of counsel is contrary to the opinions of the Supreme Court and contrary to the opinions of the other circuits.

The Brief For The United States In Opposition does not dispute the argument of the petitioner. In footnote 3, the brief in opposition admits that courts of appeals have held that where there is an evidentiary basis for the defense of reliance on advice of counsel, an instruction such as the one proposed by petitioner should be given. The brief in opposition does not cite or discuss in any way the Supreme Court decision of *United States v. Pomponio*, 429 U.S. 10 (1976), which was the basis of the court of appeals decision below. The brief in opposition impliedly admits that the court of appeals decision was in error on the law.

The brief in opposition does not cite or discuss in any way the other decisions of the Supreme Court cited by petitioner which have long established the principle that a defendant is entitled to have the trial court instruct the jury with a proper statement of the law on his theory of defense even though general instructions on "conscious participation" or "willfulness" are given. *United Brotherhood of Carpenters and Joiners of America v. United States*, 330 U.S. 395 (1947); *Bird v. United States*, 180 U.S. 356 (1901).

The Government replaced the legal issue in the petition for certiorari with an issue which argued that the facts of the case did not provide an evidentiary foundation for the giving of the advice of counsel instruction to the jury. The court of appeals did not decide that issue. The court of appeals stated that whether there was a foundation in the evidence to support the defense theory of good faith reliance was "questionable." Pet. App. A-5. The court of appeals reviewed the extensive evidence presented by both sides on the issue. The court of appeals went on to assume that there was evidence to support the defense theory of good faith reliance, and then enunciated the legal principle that "instructions on willfulness necessarily encompassed" an instruction on the defense theory of good faith reliance on the advice of counsel, which statement of the law the Government does not dispute is in error. Pet. App. A-6.

The petition must be granted to correct the erroneous statement of the law and the erroneous application of the law in this case. Whether the judgment is vacated summarily on the basis of the brief in opposition and remanded to the court of appeals or whether the petition is granted and set for further argument is within the discretion of the Court.

If the court hears further argument, it is still within the discretion of the Court to remand the case to the court of appeals to decide the issue which that Court did not decide or to decide the issue itself before a decision on the issue by the court of appeals is within the discretion of the Court.

In the event that the Court desires to decide the evidentiary foundation issue raised by the Government, the petitioner would point to the following facts which show that there was an evidentiary foundation for the instruction on good faith reliance on the advice of counsel. The principle defense of the petitioner was his reliance on the advice of counsel. He presented evidence on the issue of advice of counsel without any objection from the Government to the admission of the evidence. The Government also presented evidence on the issue of advice of counsel. Both the attorney Brown and the defendant were questioned by both the defense and by the Government attorneys on the issue of advice of counsel. There was no objection to any of the testimony. It was a fully litigated issue.

Part II of the opinion of the court of appeals gave a fairly extensive recitation of some of the evidence on both sides of the issue. Pet. App. A-5, A-6. The statement of facts in the opinion also recited evidence on the issue. Pet. App. A-2, A-3. The defendant had previously requested the advice of the attorney Alfred Brown about other tax shelters and had paid for such advice. Attorney Brown and the attorneys in his office were in the business of rendering advice on income tax shelters. The defendant sought the advice of the attorney about another tax shelter, and was advised by the attorney that the SMFA tax shelter was "superior" to the one about which the defendant inquired. The attorney was the one who recommended the SMFA tax shelter to the defendant. On the attorney's advice, the defendant actually purchased the tax shelter himself and recommended the tax shelter to his clients. Attorney Brown or one of the attorneys in his office was always present at all of the closings of the tax shelter investments. The attorney advice in this case was much more substantial then in other cases raising the defense of good faith reliance on the advice of counsel.

The Government has argued in this case that the defendant did not pay a retainer for the attorney's advice. There is no such requirement in the law. The Government can argue to the jury that this is a fact to be considered in its decision, but it is not a

fact which prevents the giving of a proper advice of counsel instruction to the jury in order for the jury to make a proper decision.

The Government in the Brief of Opposition argues that the defendant should have known that although there was a recourse portion of the investment, the side letter agreement "effectively negated the investor's personal liability on the recourse portion of the notes." Brief In Opposition, p. 2. The letter provided a credit for unsold artwork to be applied against the recourse portion of the note. The brief in opposition states that "(t)he letter therefore made the planned deductions for the 'recourse' portion of the notes illegal since the investors were not actually at risk for that portion of the investment." The issue at trial was whether the defendant believed that the recourse portion was not "actually" a recourse portion because of the effect of the credit provided by the letter, and therefore, that the deductions were illegal. The advice of the attorneys who were in the business of reviewing tax shelters was critical on this issue.

It was not even the defendant's idea to invest in the tax shelter. It was the attorney's idea in the first place. The attorney recommended the tax shelter as superior to the one about which the defendant inquired. Attorneys from that office were always present at the closings of the tax shelters. The defendant believed in the tax shelter so much that he invested in it himself after it was recommended by the attorney.

The Government points to two pieces of evidence in its argument that the defendant knew that the tax shelters were illegal. First, it points to the evidence that the defendant was a financial advisor. Secondly, it points to the evidence that at the closings the investors were informed not to show the IRS the side letter because the tax shelter "might be in question." Pet. App. A-3. There are deductions which "might be in question" in any IRS audit. In fact, it is not unusual in any IRS audit that deductions "might be in question." The Government is permitted to argue to the jury that such evidence shows knowledge of

criminality on the part of the defendant, but the jury must be properly instructed in order for the jury to make that decision. That the defendant may rely in good faith on the advice of counsel is an important instruction on this issue. The instruction informs the jury that it is proper to consider such evidence in making their decision, and the instruction sets forth the elements of the defense of good faith reliance on the advice of counsel.

The district court recognized that it was a legitimate issue and allowed the defense to argue the issue to the jury. The court of appeals' decision adamantly stated in footnote 1 that "there is no doubt that Kelley's defense theory was presented to the jury." Pet. App. A-6. When a defense theory is presented to a jury, the jury must be instructed on the issue, or the jury can conclude that the attorney is arguing something that has no basis in the law. An argument by an attorney without any instruction from the Court as to the law is "an aggravation rather than a mitigation of the harmful effect of the Court's refusal to instruct." *United States v. Duncan*, 850 F.2d 1104, 1118 (6th Cir. 1988), quoting *United States v. Phillips*, 217 F.2d 435, 440 (7th Cir. 1954).

The Government in footnote 3 of its brief in opposition also argues that any error was harmless because the "knowingly" and "willfully" instructions "did not allow the jury to convict petitioner if it concluded that he had reasonably relied on the advice of counsel." Brief in Opposition, p. 6. That argument cites no authority. That argument is contrary to the decisions which state that the failure to instruct on the good faith reliance on the advice of counsel is an aggravation rather than a mitigation of the harmful effect. *United States v. Duncan*, *supra*; *United States v. Phillips*, *supra*. The Government argued that good faith reliance on advice of counsel was not a defense in this case. When the trial court agreed with the Government request not to instruct on the law on this primary defense, the court added support to the Government argument before the jury that good faith reliance on advice of counsel is not a

defense in this case.

The argument that the failure to instruct was harmless because general willfulness instructions were given is also contrary to the decisions of this Court that general willfulness instructions do not render harmless the failure to instruct on a valid defense theory. *United Brotherhood of Carpenters and Joiners of America v. United States*, *supra*; *Bird v. United States*, *supra*. The lack of any instruction on the defense of good faith reliance on the advice of counsel can indicate to the jury that there is no basis in the law for such a defense. The failure to give an instruction on good faith reliance on the advice of counsel also leaves it to the jury to make up its own elements of such a defense, which may be greater than or different than the elements of the law.

The argument that the failure to instruct was harmless because general willfulness instructions were given is also contrary to the additional erroneous instruction which was given allowing the jury to find that the defendant acted knowingly if the defendant had a "strong suspicion" and closed his eyes. Such instruction is in error when it does not require a "deliberate" or "willful" shutting of the eyes and an absence of actual belief in the legality of the actions. *United States v. Lanza*, 790 F.2d 1015 (2nd Cir.), *cert. denied*, 479 U.S. 861 (1986); *United States v. Arbizo*, 833 F.2d 244 (10th Cir. 1987); *United States v. C no*, 702 F.2d 370 (2nd Cir. 1985); *United States v. Jewell*, 532 F.2d 697 (9th Cir.), *cert. denied*, 426 U.S. 951 (1976).

There is no harm in properly instructing a jury. There is great harm in failing to give an admittedly proper instruction to a jury on the primary defense in the case. The petition must be granted in order to correct the improper statement of the law set forth in the opinion of the court of appeals and to give the jury deciding the issue a proper instruction of the law. Only then can the issue be properly decided by the jury.

CONCLUSION

For all of the foregoing reasons, the petition for a writ of certiorari should be granted. The court should hold that form instructions on willfulness do not necessarily encompass an instruction on good faith reliance on advice of counsel. The decision of the court of appeals should be reversed and the case remanded to the court of appeals.

Respectfully submitted,

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